



ECONOMICS

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Housing and Mortgage Dynamics: Beyond the Headlines

by Benjamin Tal and Katherine Judge

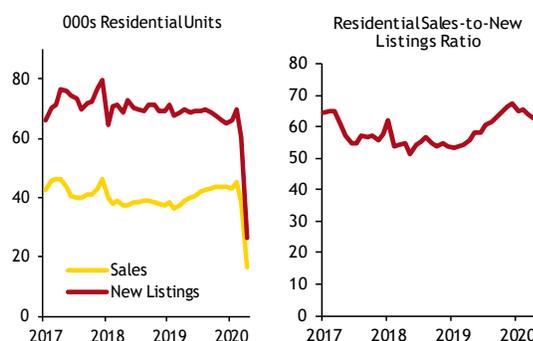
The Canadian housing market is starting to wake up. The volume of activity will rise slowly in the coming weeks, and the real shape of the market will be unveiled. Early activity already provides some hints of what we should expect.

We also look behind the scenes, using poll results* to get a better understanding of the current dynamics of the mortgage market, and a sneak peak of the characteristics of the 15% of borrowers that elected to defer mortgage payments. And while there, we also looked at the rental market, with the focus being on rent payments—who is still paying, and who isn't.

The Resale Market: Slow Awakening

The housing market was basically frozen in April. Both sales and new listings were down by just under 60%, resulting in a relatively stable sales-to-listings ratio and a muted price response (Chart 1). Naturally, all provinces experienced similar trajectories.

Chart 1
Housing Markets Froze in April

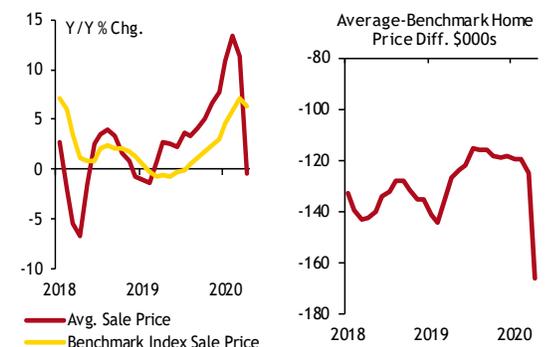


Source: CREA, CIBC

There are clear early signs that the market is starting to warm up. Activity in the first two weeks of May was notably stronger than in the first two weeks of April, and as the economy starts to open, that pace will accelerate. With the increased volume of transactions, the real shape of the market will be gradually revealed. We expect that many conflicting factors will result in a softer market (see our earlier report).

We also suggest that the housing market will see an increased divergence between mid/low priced units and the more expensive segment of the market. That trend is already evident. The Canadian Real Estate Association (CREA) uses two price indexes: an unweighted index that reports the average price as is, with no adjustments. The other index, the benchmark index, captures the price change of similar units, and therefore accounts for any compositional impact on prices. Accordingly, when the price reported by the simple index falls by more than the benchmark index, a

Chart 2
Larger Share of Less Expensive Units Behind Prices Drop (L), Gap With the Benchmark Index at Record Low (R)

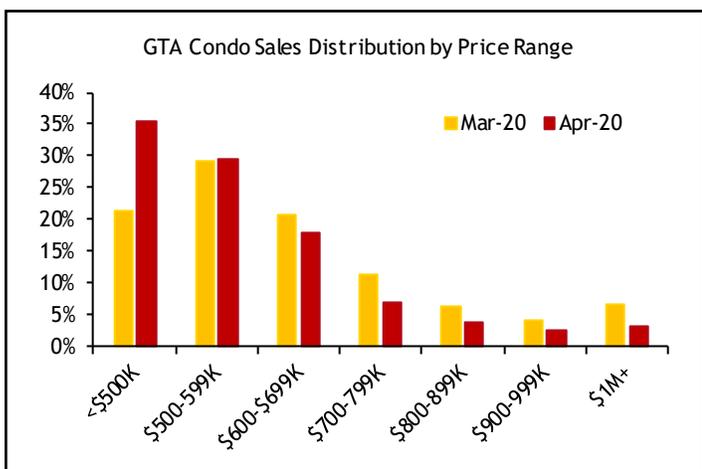


Source: CREA, CIBC

<http://economics.cibc.com>

Chart 3

April Condo Sales Concentrated in Lower Priced Units



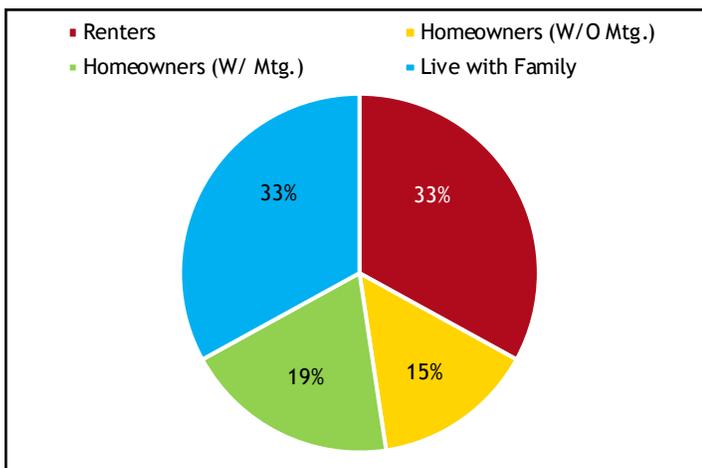
Source: Urbanation, CIBC

compositional shift towards less expensive units is occurring. And that’s exactly what we are seeing now. In fact, the gap between the two measures is currently at a record low (Chart 2). This trend in our assessment is driven primarily by demand factors.

More direct information from the GTA’s condo market shows a similar trend, with the share of condo units sold below the \$500K threshold rising notably in April to account for no less than 35% of transactions (Chart 3). Based on information received from numerous developers, that trend is consistent with what is being seen in other parts of the country, most notably in Vancouver, where inventories of larger condo units has been on the rise.

Chart 4

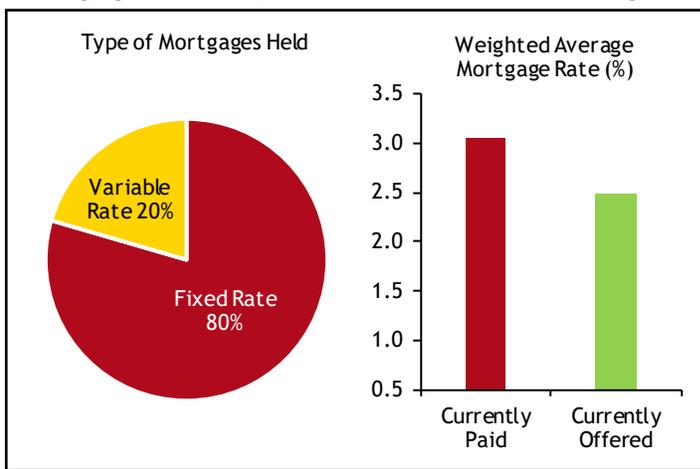
Living Arrangements



Source: CIBC Poll*, CIBC

Chart 5

Mortgages Tilted to Fixed Rate (L), Lower Mortgage Rates Open Door for Rate Resetting (R)



Source: CIBC Poll*, CIBC

The relatively strong demand for less expensive units is understandable given current economic conditions, but we believe that it also represents increased investor demand for secondary units. No less than 23% of homeowners suggested that the combination of a softer market and lower interest rates is encouraging them to consider purchasing a second unit.

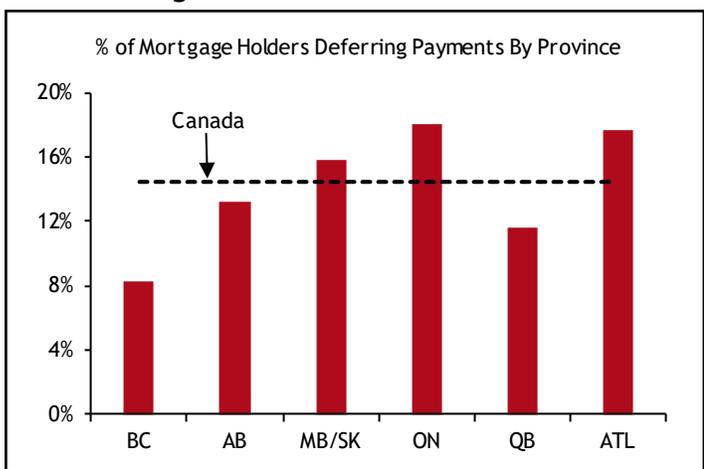
The Mortgage Market: Behind the Scenes

Zooming in on the 57% of homeowners with a mortgage in our survey (Chart 4), shows that they are heavily tilted towards fixed rates rather than variable (Chart 5, left). With the weighted average mortgage rate currently paid by borrowers being roughly 50 basis points higher than the current rate (Chart 5, right), no less than 20% of borrowers have already renegotiated their rates. We expect more to come.

The mortgage deferral program offered by Canadian banks is an essential part of the collective effort to alleviate the financial pain facing Canadian households during the crisis. So far, the uptake is roughly 15% of mortgage holders across the country, and there are clear signs that the rush is over as the number of new applications is falling steadily.

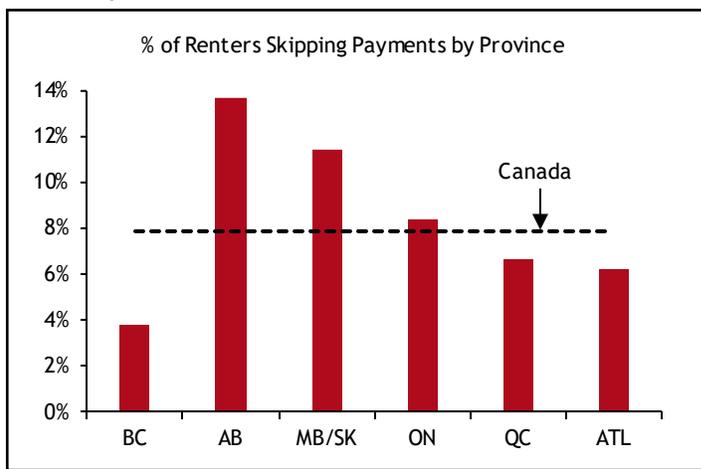
By province, the highest participation rate has been seen in Ontario, reflecting the affordability issue facing the province in general, and the GTA, in particular (Chart 6). Interestingly, BC is seeing the lowest uptake, despite being the least affordable province. In part that might reflect a higher share of alternative lenders in the province

Chart 6
Highly Indebted Ontarians Making Most Use of Deferral Program



Source: CIBC Poll*, CIBC

Chart 8
Energy Producing Provinces Seeing Highest Rent Non-Payment Rates



Source: CIBC Poll*, CIBC

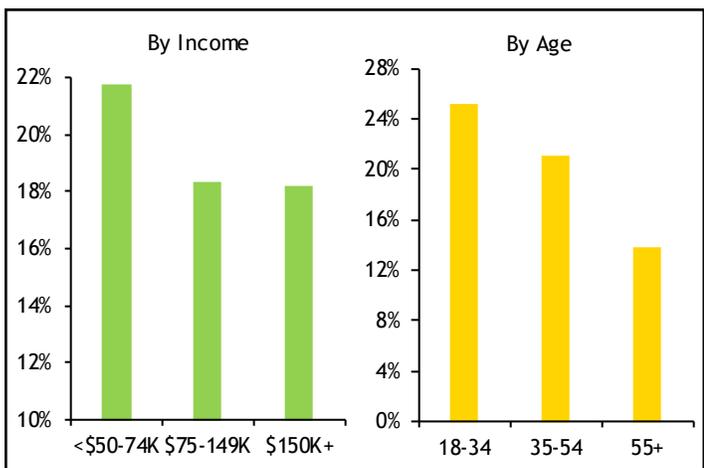
and a comparatively stronger role of foreign buyers—but we are speculating here.

Chart 7 requires less speculation as it clearly suggests that lower income borrowers are participating in the program at a higher rate, consistent with an elevated share of 18-34 years old using the program.

Zooming in on the rental segment of the market, rent collection reported by landlords averaged around 90% in both April and May, a rate that is consistent with the findings in our survey.

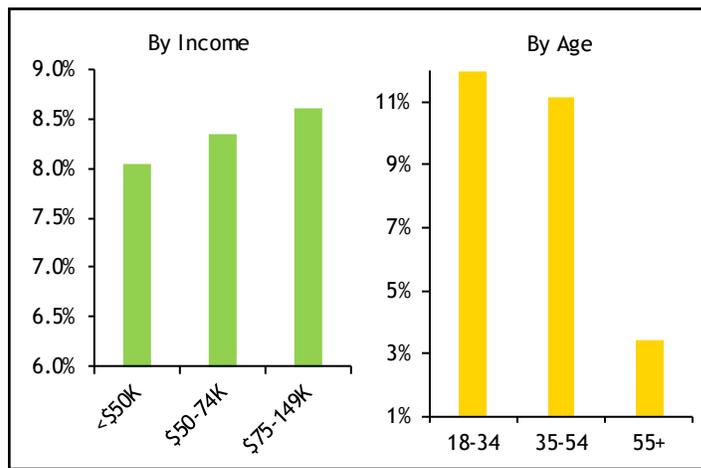
Looking across provinces (Chart 8), it's no surprise that the energy dependent prairie provinces have seen the highest rates of renters unable to pay rent given the double burden faced by both the drop in the price of oil and mass layoffs in services, particularly trade, accommodations, and food services. Although worrisome, the prairie provinces have a high homeownership rate, suggesting that the overall impact of not paying rent will be somewhat limited from a macro perspective. Ontario also stands out as having a relatively high non-payment rate, which could reflect stretched affordability in the GTA especially, which was exposed amidst layoffs in the aforementioned lower wage industries. The low rent default rate in BC likely reflects provincial policies

Chart 7
Share of Mortgage Holders Deferring Payments



Source: CIBC Poll*, CIBC

Chart 9
Composition of Renters Unable To Pay Rent

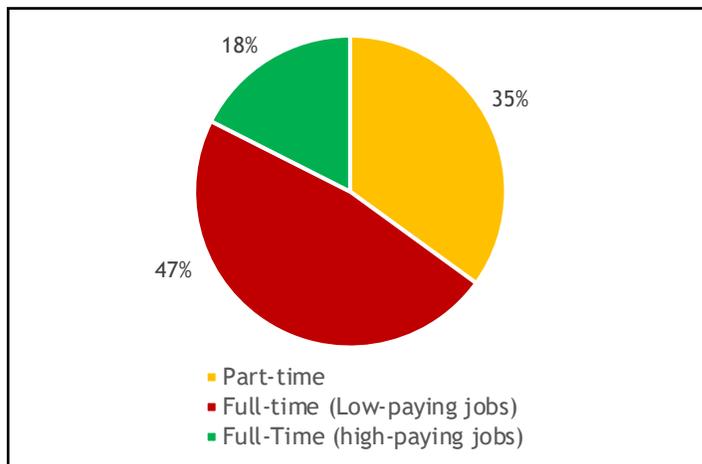


Source: CIBC Poll*, CIBC

that provide direct support for renters, in addition to the \$1,000 lump sum transfer to households that qualify.

Not only was the roughly 90% rent collection rate better than expected, the rate of low-income renters that are unable to pay rent has remained slightly lower than higher income brackets (Chart 9, left). On the surface, that might be surprising given that the vast majority of jobs lost over the past two months were in low-paying occupations (Chart 10). However, that can be explained by the fact that the income of older renters was uninterrupted in the past few months as it's based largely on pension and government transfers (Chart 9, right). Furthermore, many renters were probably able to collect CERB money which in most cases was sufficient to cover rent.

Chart 10
Contribution to Job Losses Since February



Source: Statistics Canada, CIBC

Note:

* CIBC's Covid-19 Poll: Impact on Homeownership/Buying/Selling/Renovation Intentions. Study details: From April 30th to May 5th 2020 an online survey of 1516 randomly selected Canadian adults who are Homeowners, Renters or Co-Inhabitants who are Maru Voice Canada panelists was executed by Maru/Blue. For comparison purposes, a probability sample of this size has an estimated margin of error (which measures sampling variability) of +/- 3%, 19 times out of 20. Some sample sizes are below 100.

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